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In the Supreme Court of the United States

October Term, 1957

No. 261

PEGGY LOU RIKER and FREDA H. GRASSMEE,
PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

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BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The memorandum findings of fact and opinion of the Tax Court (R. 80-96) are not officially reported. The opinion of the Court of Appeals (R. 165-191) is reported at 244 F. 2d 220.

JURISDICTION

The judgment of the Court of Appeals was entered on April 12, 1957 (R. 192), and a timely petition for rehearing was denied on June 17, 1957 (R. 193).

The petition for a writ of certiorari was filed on July 11, 1957. The jurisdiction of this Court is invoked under 28 U. S. C., Section 1254.

QUESTIONS PRESENTED

1. Whether income derived from the operation of a restaurant by taxpayer Peggy Lou Riker was income taxable to her or to a religious organization of which she was a member.

2. Whether Christ's Church of The Golden Rule, which was authorized to and did conduct business for profit through its principal temporal agency, the Elected Delegates Committee, was a corporation "organized and operated exclusively for religious * * * purposes, * * * no part of the net earnings of which inures to the benefit of any private shareholder or individual", within the meaning of Section 23(o)(2) of the Internal Revenue Code of 1939, so that contributions or gifts thereto were deductible for income tax purposes.

3. Whether taxpayer Grassmee was entitled to dependency credits for her mother in the taxable years 1948 and 1949 under Section 25(b)(1)(D) and (3) of the Internal Revenue Code of 1939.

STATUTE AND REGULATIONS INVOLVED

Section 23(o)(2), Section 25(b)(1)(D) and (3), Section 101(6) and (18) of the Internal Revenue Code of 1939, and Section 29.25-3, Section 29.101(6)-1, Section 29.101(18)-1 of Treasury Regulations 111, are set forth in the Appendix, *infra*, pp. 15-19.

STATEMENT

The findings of the Tax Court may be summarized as follows:

During the taxable years 1948 and 1949, taxpayers, Peggy Lou Riker and Freda H. Grassmee, were members of Christ's Church of The Golden Rule (hereinafter referred to as the Church), a religious nonprofit California corporation, which was organized in 1944. (R. 81, 84, 87.) The Church was adjudicated a bankrupt in 1945 and during 1948 and 1949 was in bankruptcy. (R. 81.)

The Church adopted a constitution (R. 20-30) and canon laws (R. 30-67) in 1948 (R. 81). According to its constitution (R. 22, 81-82), the economy of the Church was based upon a belief that economic equality is the only enduring foundation upon which to build industrial, business, political, national, and international relations; and that to insure such equality (R. 22)—

> the property and earnings of the individual members of the Church should be owned and managed by the Church for the benefit of all mankind in accordance with the rules and regulations of the ecclesiastical society of this Church, that God may be glorified and all mankind directly or indirectly benefited.

The ecclesiastical affairs of the Church were in the hands of an organization consisting of a Senior Elder, an Advisory Board of Elders, and College of Pastors. (R. 23-26, 82.) The temporal affairs of the Church were in the hands of "temporal agencies," subject to the ultimate control of the ecclesiastical authorities.

Such affairs were carried on through charters granted by the Senior Elder, with the advice of the Advisory Board, "to the various congregations, projects and other temporal activities * * *." (R.26-27, 82.)

According to the canon laws of the Church, a charter could be granted, withheld, or revoked upon whatever terms and conditions the Church government designated. (R. 82.) Those laws provided (R. 33, 38, 82), *inter alia*, that all temporal agencies "shall hold their property upon a private trust for the ecclesiastical organization," and that (R. 38)—

> All transfers, conveyances and sales shall be presumed to be bona fide gifts to the Lord's work unless there be conditions or understandings or promises to the contrary in writing duly approved in writing by the duly constituted ecclesiastical Church Government.

In operation, activities of Church members were of two types. Some members devoted all of their time to working in Church projects and studying to be ministers of the Church's teachings. These student ministers lived in apostolic societies called "Student Minister Training Projects." One purpose of these projects, most of which were engaged in commercial activities, was to spread the teachings of the Church by having the public witness the application of these teachings in everyday life. Some projects were not engaged in commercial activities but simply operated residential facilities for Church members. Members living in both types of projects contributed their earnings to the Church. Other Church mem-

bers lived at home and participated in Church activities. The Church operated a theological seminary. (R. 48, 82-83.)

The principal temporal agency of the Church was the Elected Delegates Committee (the Committee) which was formed in 1946. (R. 83.) During 1948 and 1949, the Committee operated various student minister training projects. It also operated the Church treasury and carried on various commercial activities in competition with privately owned enterprises, including, among others, a restaurant, a laundry, a lumber yard, bulb gardens, farming, stock raising, and a warehouse. These enterprises were operated for profit. Gross receipts from the operation of these projects were sent to the Committee, covered by a form stating that the transfer was an outright gift from the project manager and was to be used only for Church purposes. (R. 83.)

For 1948 and 1949, the Committee filed amended returns of income on Treasury Department Form 990 as an organization exempt under Section 101 of the Internal Revenue Code of 1939, and also amended returns as an apostolic society on the partnership Form 1065. The returns showed the Committee's gross income for 1948 as $484,981.44, of which $347,489.99 was reported as received from the operation of student minister training projects, and $137,491.45 from contributions and gifts. In 1949, gross income of $409,590.05 was reported, of which $352,528.70 was from the operation of student minister training projects, and $56,033.27 was from gifts and contributions. On the Committee's returns as an

apostolic society, the undistributed pro rata share of each member of the apostolic society was reported as $342.27 for 1948 and $316.17 for 1949. (R. 83-84.)

Prior to joining the Church, taxpayer Peggy Lou Riker and her husband had operated a drug store in partnership with the latter's parents. The partnership was dissolved and Peggy Lou Riker and her husband acquired the fixtures and used them to set up a student minister training project to operate a restaurant under the name of "Your Food Fountain" (sometimes called the Fountain). Mrs. Riker was manager of the project and the business license was in her name. Her duties included giving religious instructions to "members" of the project, who varied in number from 12 to 17. All of the receipts from the operation of the Fountain were turned over to the Committee on a form signed by Mrs. Riker as project manager. Funds were in turn allocated by the Committee from the Church treasury for the operation of the Fountain and the living expenses of the members of the group. (R. 84-85.)

While the bankruptcy proceedings of the Church were pending, Mrs. Riker sued the trustees in bankruptcy to establish her ownership of the equipment of the Fountain. An agreement was made in May 1947, between Mrs. Riker and the trustees, relating to the Fountain while the litigation was pending, which provided that Mrs. Riker was to operate the establishment until the lawsuit involving ownership was settled. The income during this period was to belong to her and she was to pay the trustees certain amounts to be deposited by the trustees in a

trust fund account. All operating expenses were to be paid by her. (R. 85.)

From May 1947 until July 1948, the restaurant was operated under this agreement. Of this period, from May 1947 until January 1948, the restaurant was run as a "Church project," and the earnings were turned over to the Committee by Mrs. Riker. From January 1948 until June 1948, she ran the business in private partnership with other persons who were not members of the Church, and from June until September 1948, she operated the business on a percentage basis with a prospective purchaser of the business. Her partnership share of the restaurant's earnings was contributed to the Committee. For five months of her fiscal year 1948, January 20 to June 30, Mrs. Riker filed partnership returns for three different partnerships that operated the restaurant in this period. In July 1948, the assets of the restaurant were sold to the Committee for $1,500. Mrs. Riker consented to the sale. (R. 85-86.)

Mrs. Riker filed an income tax return for her fiscal year 1948 (October 1, 1947, until September 30, 1948), which disclosed a net profit of $7,568.25 from the operation of a restaurant business under the name of "Your Food Fountain." (R. 86.) A memorandum attached to the return read as follows (R. 86-87):

> ITEM 2. WAGES, ETC.
>
> Taxpayer was employed by Own Business for a gross income of $8959.11 during the taxable year. However, under the rules of the apostolic

society (of which taxpayer is an associate) that all in the society share their income, $8959.11 was contributed to and became a part of the income of the apostolic society, and is reported as part thereof. Taxpayer would therefore be taxed twice on the same income by reporting it as wages and also as a dividend. For this reason, this latter sum is reported only as part of the dividend or taxpayer's pro rata share of the net income of said apostolic religious society. (See Item No. 3 Dividends).

ITEM 3. DIVIDENDS

1/575 interest in $217,001.54 net income of the Elected Delegates' Committee of the Ecclesiastical Society of Christ's Church of The Golden Rule, an Apostolic Religious Association, for its accounting period of Oct. 1, 1947 to Oct. 1, 1948. This was not received as a dividend, but is reported under Sec. 101(18)—Per person in Association $377.39.

Number of persons in taxpayer's family who were in association and obtained support from Society during period:

2 times $377.39.....$754.78

In her return for 1948, Mrs. Riker claimed the sum of $8,959.11 as a deductible contribution to the Church. This claim was disallowed by the Commissioner and this action was alleged as error in the original petition. In an amended petition, it was prayed that the income of the Fountain be found to be the income of the Church. (R. 87.)

Taxpayer Freda H. Grassmee was employed in a law office in Los Angeles during 1948 and 1949, and

contributed practically all of her salary for those years to the Committee. She and her mother lived in a Church residential project and participated in religious activities of the Church. Both received their support from the Church. Freda's income tax returns for 1948 and 1949 contained memoranda as to the disposition of her income similar to that attached to Mrs. Riker's return. On her returns for both years, she claimed a dependency exemption for her mother. (R. 87.)

The Commissioner disallowed the deductions claimed as contributions to the Church in 1948 and 1949. In an amended answer, he claimed increased deficiencies based on disallowance of the dependency credits claimed for Freda's mother. (R. 88.)

The Tax Court sustained the Commissioner's determinations and held (1) that the income derived from the operation of the Fountain by Mrs. Riker was her income and not that of the Church organization to which she contributed it (R. 88-89); (2) that no part of the amounts contributed to the Church by the taxpayers was deductible as a contribution to a religious organization since the Church was not organized and operated exclusively for religious purposes within the meaning of Section 23(o) of the Internal Revenue Code of 1939 (R. 91-95); and (3) that taxpayer Freda H. Grassmee was not entitled to a dependency exemption for her mother since her support was received from the Church. (R. 96.) The Court of Appeals affirmed the decision of the Tax Court.

ARGUMENT

1. The three issues presented to the court below all involved questions of fact, and, as the Court of Appeals stated (Pet. App. 26; R. 183), the record supports the findings of the Tax Court with respect to those issues. A well settled rule of this Court makes concurrent findings of two courts below final in the absence of exceptional error. *Comstock* v. *Group of Investors*, 335 U. S. 211, 214. Taxpayers having failed to demonstrate that exceptional error was committed, there is no warrant for review by this Court of the factual findings which are dispositive of the case.

On the facts, the courts below found (1) that the restaurant business, known as Your Food Fountain, was owned and operated by taxpayer Riker rather than the Church of which she was a member and that the income therefrom belonged to her; (2) that, for the taxable years involved, neither she nor taxpayer Grassmee was entitled to a 15% deduction from gross income under Section 23(o) of the Internal Revenue Code of 1939 (Appendix, *infra*, p. 15) by virtue of the fact that Riker turned the receipts from the business over to the Committee for the exclusive use of the Church, and Grassmee did the same with her salary, since neither the Church nor the Committee qualified as a religious organization so as to render contributions or gifts thereto deductible; and (3) that taxpayer Grassmee was not entitled to a dependency credit for her mother under Section 25 (Appendix, *infra*, pp. 15-16).

As for the first point, the Court of Appeals listed eleven substantial reasons in support of its conclusion sustaining the Tax Court's finding that the income from the restaurant business belonged to taxpayer Riker, and not to the Church. (Pet. App. 16-18; R. 176-177.) Mrs. Riker has not sought to controvert those reasons. In addition, it is to be noted that in her return for the fiscal year 1948, as well as in her original petition in the Tax Court, she took the position that income from the operation of the restaurant was her income and not that of the church organization to which she contributed it. (R. 15, 86-87.)[1]

With respect to the second point, the Court of Appeals pointed out that neither the Church nor the Committee met any one of the three conditions which would be necessary to make contributions deductible under Section 23(o)(2), since neither was "organized and operated exclusively for religious * * * purposes" and various members of the Church shared in the benefits of its net earnings. See Pet. App. 18-

[1] By an amended petition, Mrs. Riker claimed that the receipts from the business belonged to the Church Committee, an alleged religious or apostolic society under Section 101(18) (Appendix, *infra*, pp. 16-17) of the Internal Revenue Code of 1939, and hence that she was taxable on only her *pro rata* share of the net income of the Committee. (R. 68-71, 87.) This point was not passed upon by the Tax Court, and although the Court of Appeals held (R. 182) that the Church would not fall within the exemptive provisions of Section 101(18), it characterized its remarks in so concluding as "gratuitous" since it had already concluded that the restaurant was a personal and individual venture rather than a Church activity. (Pet. 26; R. 182).

24. The constitution (R. 26-28) and canon laws (R. 33-34) contemplated and authorized the Church to engage in temporal and business affairs; the Committee was an agency entirely controlled by the Church (R. 26, 34) and was created solely for temporal and business purposes (R. 92); and the record shows that, in fact, a wide scope of commercial activities and projects were operated by the Church through its Committee.[2] Although the taxpayers claimed that these projects and activities were intended to promote and foster spiritual and religious purposes and teachings of the Church, both the Tax Court and the Court of Appeals observed (R. 95, 178; Pet. App. 19) that the very means chosen by the Church to attain its spiritual purpose involved engaging in commercial activities through its principal temporal agency, the Committee. Furthermore, contrary to the requirement of Section 23(o)(2), individual members of the Church indisputably shared in its net earnings in that homes and subsistence were provided for them out of the Church treasury. (R. 84, 86-87, 118-119, 122-123, 125, 147-148, 178; Pet. App. 19, 24.)

Thirdly, the right of taxpayer Grassmee to a dependency credit for her mother during the taxable years 1948 and 1949 under the provisions of Section

---

[2] The Tax Court found (R. 83) that the Committee, which operated these projects, carried on various commercial activities in connection with privately owned enterprises, including, among others, a restaurant, a laundry, a lumber yard, bulb gardens, farming, stock raising and a warehouse.

25(b)(1)(D) and (3) (Appendix, *infra*, pp. 15-16) is entirely a factual matter. The Tax Court found that "Freda did not contribute over half of the support of her mother," who lived "in a Church project and received her support directly from the Church" (R. 96); the court below agreed (Pet. App. 26).

2. Since the petition does not contain a "direct and concise argument" setting forth the reasons relied on for the allowance of the writ, as required by Rule 23-1(h) of the Rules of this Court, it is not clear on what basis review is sought. In large part, the petition merely attempts to reargue the facts of this case, already determined adversely to the taxpayers by the two courts below. To the extent that the petition does attempt to present general issues of law, we would point out that such general legal questions are not reached in this case because the concurrent findings of fact are dispositive, on any theory of the applicable legal rules. The case simply does not present any of the general legal issues with respect to the taxation of charitable organizations with which the courts have been concerned. In any event, in view of the change in the tax law relating to charitable organizations since the taxable years involved in this case, we submit that, as suggested in our brief in opposition in *The John Danz Charitable Trust* v. *Commissioner of Internal Revenue*, No. 145, October Term, 1956, certiorari denied, 352 U.S. 828, the general issues of law under the comprehensive legislation effective for taxable years after 1950 should be determined in cases arising under those new provisions.

CONCLUSION

It is respectfully submitted that the petition for a writ of certiorari should be denied.

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AUGUST, 1957.

APPENDIX

Internal Revenue Code of 1939:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * *

(o) *Charitable and Other Contributions.*—In the case of an individual, contributions or gifts payment of which is made within the taxable year to or for the use of:

* * * *

(2) [as amended by Section 224(a) of the Revenue Act of 1939, c. 247, 53 Stat. 862] A corporation, trust, or community chest, fund, or foundation, created or organized in the United States or in any possession thereof or under the law of the United States or of any State or Territory or of any possession of the United States, organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, and no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation:

* * * *

(26 U.S.C. 1952 ed., Sec. 23(o).)

SEC. 25. CREDITS OF INDIVIDUAL AGAINST NET INCOME.

* * * *

(b) [as amended by Section 10(b) of the Individual Income Tax Act of 1944, c. 210, 58 Stat. 231; Section 102(a) of the Revenue Act of 1945, c. 453, 59 Stat. 556; and Section 201 of

the Revenue Act of 1948, c. 168, 62 Stat. 110]
Credits for Both Normal Tax and Surtax.—

(1) *Credits.*—There shall be allowed for the purposes of both the normal tax and the surtax, the following credits against net income:

* * * *

(D) An exemption of $600 for each dependent whose gross income for the calendar year in which the taxable year of the taxpayer begins is less than $500, * * *

* * * *

(3) *Definition of Dependent.*—As used in this chapter the term "dependent" means any of the following persons over half of whose support, for the calendar year in which the taxable year of the taxpayer begins, was received from the taxpayer:

* * * *

26 U.S.C. 1952 ed., Sec. 25(b).)

SEC. 101. EXEMPTIONS FROM TAX ON CORPORATIONS.

The following organizations shall be exempt from taxation under this chapter—

* * * *

(6) Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, and no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation;

* * * *

(18) Religious or apostolic associations or corporations, if such associations or cor-

porations have a common treasury or community treasury, even if such associations or corporations engage in business for the common benefit of the members, but only if the members thereof include (at the time of filing their returns) in their gross income their entire pro-rata shares, whether distributed or not, of the net income of the association or corporation for such year. Any amount so included in the gross income of a member shall be treated as a dividend received.

* * * *

(26 U.S.C. 1952 ed., Sec. 101(6) and (18).)

Treasury Regulations 111, promulgated under the Internal Revenue Code of 1939:

Sec. 29.25-3 [as amended by T.D. 5517, 1946-2 Cum. Bull. 8, 15, and T.D. 5687, 1949-1 Cum. Bull. 9, 19]. *Personal exemption, surtax exemptions, and exemptions for both normal tax and surtax.*—

* * * *

(d) *Taxable years beginning after December 31, 1947.*— * * *

* * * *

(5) *Exemptions for dependents.*—Section 25(b)(1)(D) allows to a taxpayer an exemption of $600 for each dependent whose gross income for the calendar year in which the taxable year of the taxpayer begins is less than $500, who receives more than one-half of his support from the taxpayer for such calendar year and who does not file a joint return with his spouse. * * *

* * * *

Sec. 29.101(6)-1. *Religious, Charitable, Scientific, Literary, and Educational Organizations and Community Chests.*—In order to be exempt under section 101(6), the organization must meet three tests:

(1) It must be organized and operated exclusively for one or more of the specified purposes;

(2) Its net income must not inure in whole or in part to the benefit of private shareholders or individuals; and

(3) It must not by any substantial part of its activities attempt to influence legislation by propaganda or otherwise.

* * * * *

Since a corporation to be exempt under section 101(6) must be organized and operated exclusively for one or more of the specified purposes, an organization which has certain religious purposes and which also manufactures and sells articles to the public for profit, is not exempt under section 101(6) even though its property is held in common and its profits do no inure to the benefit of individual members of the organization. * * *

* * * * *

Sec. 29.101(18)-1 [as amended by T.D. 5158, 1943 Cum. Bull. 45, 47, and T.D. 5600, 1948-1 Cum. Bull. 5, 6]. *Religious or Apostolic Associations or Corporations.*—Religious or apostolic associations or corporations are exempt from taxation under chapter 1 if they have a common treasury or community treasury, even though they engage in business for the common benefit of the members, provided each of the members includes (at the time of filing his return) in his gross income his entire pro rata share, whether distributed or not, of the net income of the association or corporation for the taxable year of the association or corporation ending with or during his taxable year. Any amount so included in the gross income of a member shall be treated as a dividend received.

Every association or corporation claiming exemption as a religious or apostolic association or corporation under the provisions of section 101

(18) and this section shall make for each taxable year a return on Form 1065 * * * stating specifically the items of its gross income and deductions, and its net income, and there shall be attached to the return as a part thereof a statement showing the name and address of each member of the association or corporation and the amount of his distributive share of the net income of the association or corporation for such year. If the taxable year of any member is different from the taxable year of the association or corporation, the distributive share of the net income of the association or corporation to be included in the gross income of the member for his taxable year shall be based upon the net income of the association or corporation for the taxable year of the association or corporation ending within the taxable year of the member.